

AR61

Winspear Business Reference Room  
University of Alberta  
1-18 Business Building  
Edmonton, Alberta T6G 2R6

**BXL**  
ENERGY LTD.

1996

Annual

Report



# Highlights

Winspear Business Reference Room  
University of Alberta  
1-18 Business Building  
Edmonton, Alberta T6G 2R6

years ended December 31,	1996	1995	% Change
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## FINANCIAL (thousands, except per share data)

Oil and gas sales	\$ 1,775	\$ 684	160
Gas management contract fees	\$ 946	\$ 354	167
Cash flow from operations	\$ 1,349	\$ 463	191
Per share	\$ 0.09	\$ 0.03	200
Net earnings	\$ 571	\$ 214	167
Per share	\$ 0.04	\$ 0.02	100
Capital expenditures	\$ 4,258	\$ 2,156	97
Long-term debt	\$ 1,612	\$ 1,139	42

## OPERATING

### Production

Oil and NGLs (bbls per day)	143	77	86
Gas (mcf per day)	478	97	393
Equivalent barrels (boe per day)	191	87	120

### Reserves

#### Proven

Oil and NGLs (mbbls)	279	224	25
Gas (mmcf)	7,920	1,807	338
Equivalent barrels (mboe)	1,071	404	165

#### Proven and Probable

Oil and NGLs (mbbls)	566	289	96
Gas (mmcf)	12,800	3,577	258
Equivalent barrels (mboe)	1,846	646	186

### Undeveloped land (acres)

Gross	55,848	54,040	3
Net	13,540	8,681	56

## SHARE DATA

### Number (thousands)

Weighted average outstanding	14,261	13,477	6
Outstanding at year end	16,999	13,599	25
Fully diluted at year end	20,037	16,527	21

### Trading price (per share)

High	\$ 0.70	\$ 0.50	40
Low	\$ 0.30	\$ 0.26	15
Close	\$ 0.60	\$ 0.34	76

Shares traded (thousands)	2,106	352	498
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The past year was one of high activity levels and considerable achievement for BXL. During 1996, we posted gains in almost every area of our business.

### Growth Strategy

BXL's goal is to increase shareholder value by finding and producing high quality crude oil and natural gas reserves at low cost. Reducing risk through the effective employment of resources is a cornerstone to achieving this goal. Our strategy is to increase the efficiency of BXL's

DURING 1996, BXL BUILT THE FOUNDATION OF A SUCCESSFUL OIL AND GAS EXPLORATION AND PRODUCTION COMPANY. WE ENTERED 1997 WITH A SUBSTANTIAL PORTFOLIO OF PROPERTIES CONCENTRATED IN THREE WELL-DEFINED AREAS, AN EXPERIENCED MANAGEMENT TEAM, A SOLID PRODUCTION BASE AND MOST IMPORTANTLY, THE GROWTH OPPORTUNITIES TO TAKE US INTO THE FUTURE.

resources by maintaining a balance of acquisitions and drilling within well-defined geographic areas. BXL targets areas in which it has a strong understanding of the geology and operating characteristics. To be considered for investment an area must have the capability to double or triple existing production and reserves through low risk

operations such as tying in non-producing reserves, re-completions and drilling. In addition, the area should have reasonable access to infrastructure such as roads, pipelines and processing facilities.

Development of a successful core area starts with a strategic acquisition which could involve relatively minor working interests. Once an initial foothold has been established, BXL moves quickly to exploit missed opportunities, consolidate our interests, acquire additional exploratory acreage and increase control within the area.

### 1996 in Review

We completed the year with a substantial portfolio of properties, concentrated in the Tweedie, Wilson Creek/Westerose and Gift/Little Horse areas of Alberta. These areas provide BXL with a solid, high quality oil and gas production base and substantial growth opportunities through undeveloped lands. Highlights of the year include:

- Established a new core area at Wilson Creek/Westerose and dramatically expanded interests at Tweedie.
- Increased average daily production by 120 percent to 191 barrels of oil equivalent per day and exited the year producing 290 barrels of oil equivalent per day.
- Increased capital expenditures by 97 percent to \$4,258,000, of which approximately \$2,203,000 was devoted to property acquisitions.
- Ended the year with proven plus probable reserves of 1.85 million barrels of oil equivalent, an increase of 186 percent over last year.
- Improved net undeveloped acreage position by 56 percent to 13,500 acres.
- Increased cash flow to \$1,349,000 (0.09 per share) from \$463,000 (\$0.03 per share) in 1995 while net earnings increased to \$571,000 (\$0.04 per share) from \$214,000 (\$0.02 per share).

PRODUCTION  
(boe per day)



- Traded 2.1 million shares ranging from a low of \$0.30 per share to a high of \$0.70 per share and closed the year at \$0.60 per share.
- Raised \$1,850,000 through the issuance of 3,400,000 shares at prices ranging from \$0.45 to \$0.67 per share.
- Participated in the drilling or recompleting of 8 gross (2.4 net) wells resulting in 2 gas (0.7 net) wells, 2 oil (0.3 net) wells, 2 suspended (1.1 net) wells and 2 (0.3 net) abandonments.
- Generated cash flow of \$946,000 from gas management contracts (\$412,000 in 1995), primarily as a result of strong eastern United States gas markets during the first half of the year.

### Outlook

We are pleased with our progress to date in 1997. At Tweedie, we expect three additional gas wells to be placed on production during the second quarter, raising our total gas production from the area to 3.25 million cubic feet per day. Opportunities exist in the area for additional acquisitions and development drilling.

During the first quarter of 1997, BXL recompleted a gas well at Wilson Creek which has added approximately 400 thousand cubic feet of natural gas and 18 barrels of natural gas liquids to our daily production. BXL holds an interest in offsetting mineral rights and expects to earn additional interests as a result of recent negotiations. Up to five wells may be drilled in the Wilson Creek/Westerose area during 1997.

At Gift/Little Horse, we have entered into several agreements under which at least three wells are planned to be drilled. Several other prospective locations have been identified, which could result in three additional wells in late 1997.

BXL completed the first quarter of 1997 producing approximately 350 barrels of oil equivalent per day and expects to reach 700 barrels of oil equivalent per day by mid year. Based on our existing property portfolio, we have set an aggressive yet achievable 1997 target exit rate of 1,000 barrels of oil equivalent per day. During 1997, we will continue to evaluate acquisitions which will add to reserves and production in ever increasing increments.

We appreciate the efforts of our dedicated employees and consultants and thank the Board of Directors for their advice and support.

Sincerely,

Bruce G. McIntyre  
President

Michael J. Makinson  
Vice President, Finance

David B. Savage  
Vice President, Land

April 11, 1997

During 1996, BXL increased its production, reserves and undeveloped acreage position in the Tweedie, Wilson Creek/Westerose and Gift/Little Horse areas. Overall average production increased to 191 barrels of oil equivalent per day compared to 87 barrels of oil equivalent per day in 1995. In December 1996, BXL's average daily production was 290 barrels of oil equivalent. The increases were due primarily to 12 months of production from the Gift/Little Horse area compared to three months in 1995, the Wilson Creek acquisition effective July 1996 and the commencement of gas production from Tweedie in November.



**TWEEDIE IS CHARACTERIZED BY SHALLOW GAS WITH LOW RISK DEVELOPMENT POTENTIAL.**

**WILSON CREEK/WESTEROSE HAS OIL AND LIQUIDS-RICH GAS PRODUCTION AND HOSTS MULTI-ZONE DRILLING OPPORTUNITIES WITH YEAR-ROUND ACCESS.**

**GIFT/LITTLE HORSE IS A HIGH POTENTIAL, LIGHT OIL PROPERTY WITH OPPORTUNITIES TO EXPAND OWNERSHIP IN LANDS AND INFRASTRUCTURE.**

## Well Activity

	1996		1995	
	Gross	Net	Gross	Net
Gas	2	0.7	1	0.4
Oil	2	0.3	—	—
Suspended	2	1.1	2	1.5
Dry	2	0.3	—	—
Total	8	2.4	3	1.9

Successful gas wells were drilled at Tweedie and Westerose. The Tweedie well is on production and the Westerose well will be tied in at a later date. At Gift/Little Horse, BXL drilled five wells and recompleted one well during 1996, resulting in two oil wells, two suspended wells which require further evaluation and two abandonments. During 1997, BXL plans to drill up to 10 wells, primarily in the Gift/Little Horse and Wilson Creek/Westerose areas.

## Land Holdings (acres)

	Developed		Undeveloped		Total	
	Gross	Net	Gross	Net	Gross	Net
Tweedie	12,800	8,311	3,200	2,432	16,000	10,743
Wilson Creek/Westerose	12,160	2,075	7,520	2,444	19,680	4,519
Gift/Little Horse	5,440	729	34,720	6,253	40,160	6,982
Other	5,120	674	10,408	2,411	15,528	3,085
Total	35,520	11,789	55,848	13,540	91,368	25,329

Undeveloped acreage included with the Tweedie and Wilson Creek acquisitions plus Crown land sales were the main contributors to the 56 percent increase in our net undeveloped land position to 13,540 acres, up from 8,681 acres in 1995.

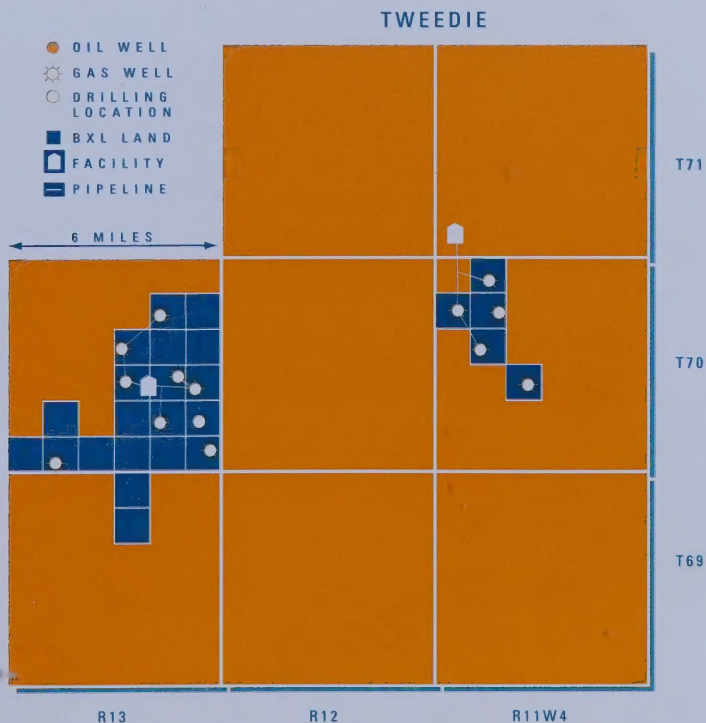
## Tweedie

The Tweedie area is located approximately 180 kilometres northeast of Edmonton, Alberta near Lac La Biche. Area wells are typically 450 metres deep and produce sweet natural gas from one or two zones with productivity ranging from 300 to 800 thousand cubic feet per day. Success in this area is dependent on a large land position and access to pipeline and compression facilities.

During 1996, BXL expanded its Tweedie interests from a 40 percent interest in 12 sections of land and 5 shut-in gas wells to an average 67 percent interest in 25 sections of land, net production of 450 thousand cubic feet per day and 11 shut-in gas wells. During March 1997, BXL completed the construction of a pipeline to tie in two of the shut-in wells and net production increased to one million cubic feet per day. BXL is currently constructing a second compression facility and gas gathering system to tie in three of the five wells on the east side of the project area. These wells are expected to come on-stream during the second quarter of 1997 when net production from the area will increase to 3.25 million cubic feet of natural gas per day.

BXL will drill and tie in additional wells as capacity becomes available and continues to identify growth opportunities in the area. BXL is also evaluating methods of increasing production and reserves on existing lands. Nearby competitors have recently introduced techniques such as reduced spacing and horizontal drilling to increase the drainage of natural gas reserves. BXL will monitor the effectiveness of these programs during 1997.

INFRASTRUCTURE EXPANSION COMBINED  
WITH A LARGE UNDEVELOPED LAND BASE  
WILL ALLOW BXL CONTINUED DEVELOPMENT  
IN THIS AREA THROUGH 1997 AND 1998.



## Wilson Creek/Westerose

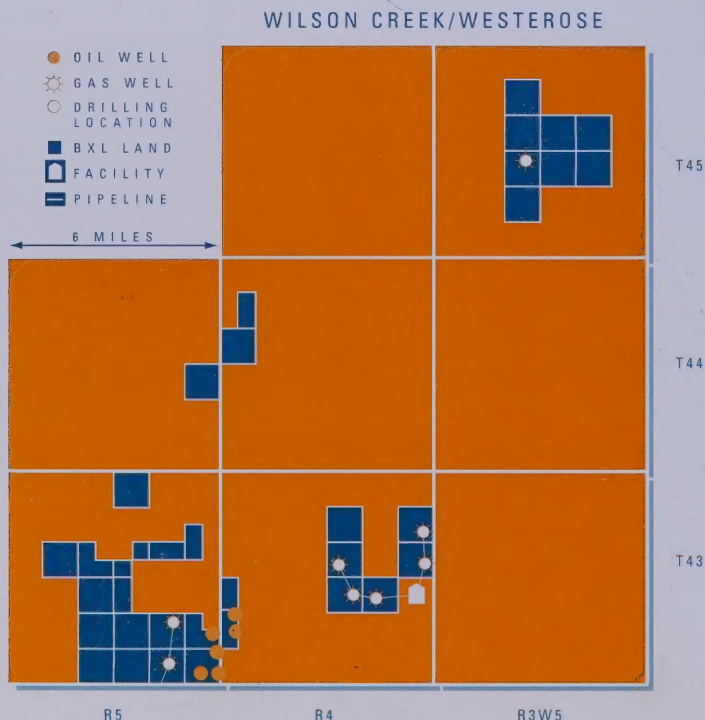
Wilson Creek/Westerose is located approximately 200 kilometres north of Calgary, Alberta. This is an area characterized by long-life reserves of light gravity oil and liquids-rich natural gas, access to processing facilities and multi-zone potential.

In mid 1996, BXL completed its first acquisition at Wilson Creek which included production of 53 barrels of oil equivalent per day, interests in gathering and compression facilities and 19,500 gross (4,800 net) acres of developed and undeveloped land. BXL quickly increased its land inventory by acquiring interests in an additional 2,240 gross (1,260 net) acres of undeveloped land. Throughout 1996, BXL added to its Wilson Creek/Westerose interests, exiting the year with production of 100 barrels of oil equivalent per day and interests in 7,500 (2,400 net) acres of undeveloped land. Early

in 1997, BXL completed 1 (0.7 net) well in the Belly River Formation which is producing approximately 85 (58 net) barrels of oil equivalent per day. By mid year 1997, we expect Wilson Creek production to be 160 barrels of oil equivalent per day.

**SUBSTANTIAL RESERVE ADDITIONS ARE POSSIBLE IN THE WILSON CREEK/WESTEROSE AREA. BXL PLANS ON DRILLING UP TO FIVE WELLS IN 1997.**

BXL has successfully negotiated farm-ins on several blocks of undeveloped land with plans to drill three to five wells during 1997. BXL continues to identify and negotiate acquisition opportunities in Wilson Creek/Westerose and projects strong reserve additions within this area during 1997.



## Gift/Little Horse

Gift/Little Horse is located approximately 300 kilometres northwest of Edmonton, Alberta just north of Lesser Slave Lake. The area is characterized by wells producing light gravity, sweet crude oil at rates of up to 300 barrels per day from the Devonian-aged Gilwood sandstone. Wells are 1,800 to 2,000 metres deep and the area can be accessed throughout most of the year. BXL has interests in 63

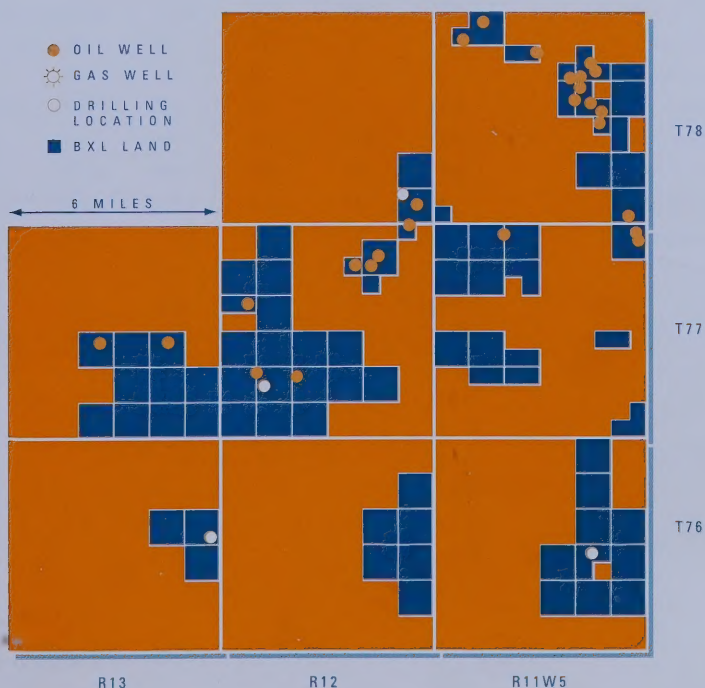
sections of undeveloped acreage and proprietary rights to 65 square miles of 3-D seismic data.

BXL made its initial acquisition in the Gift/Little Horse area in September 1995. During 1996, BXL participated in drilling/recompleting 6 wells in the area, resulting in 2 (0.3 net) oil wells, 2 (1.1 net) suspended wells and 2 (0.3 net) dry holes. Higher

than anticipated operating costs in 1996 are being addressed by connecting wells to facilities where possible and shutting in marginal producers.

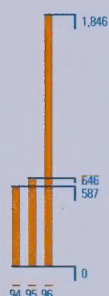
In the first quarter of 1997, Gift/Little Horse production is expected to average 120 barrels per day. Although the high demand for drilling rigs has delayed a portion of our program to the summer, BXL plans to drill or recomplete up to seven wells in the area during 1997. To date, two recompletions have resulted in 1 (0.7 net) oil well and 1 (0.6 net) oil well requiring further evaluation. Drilling will include up to five seismically defined locations on acreage directly offsetting producing oil wells. Some of these wells will result in BXL earning additional interests as a result of optioning lands considered to be the most perspective.

### GIFT/LITTLE HORSE



## Oil and Gas Reserves

RESERVES  
(proven plus probable)  
(mboe)



BXL's oil and gas reserves were evaluated by Gilbert Laustsen Jung Associates Ltd. effective January 1, 1997 using the pricing assumptions summarized on the following page. Based on their report, BXL's share of oil and natural gas liquids reserves increased 25 percent during 1996 to 279 thousand barrels on a proven basis and 96 percent to 565 thousand barrels on a proven plus probable basis. Reserve increases occurred at Wilson Creek and to a lesser extent, Gift/Little Horse.

Proven natural gas reserves were 7.9 billion cubic feet at year end 1996, an increase of 338 percent over 1996 levels and proven plus probable gas reserves increased 258 percent to 12.8 billion cubic feet. The majority of the natural gas reserves were added at Tweedie and Wilson Creek.

### Reserves (at January 1, 1997)

Reserve category	Company Interest Reserve Before Royalty			Estimated Before Tax Present Value of Future Net Revenue (thousands)		
	Oil & NGLs (mbbls)	Gas (mmcf)	BOE (mboe)	Discounted at		
				10%	15%	20%
Proven producing	248	2,030	451	\$ 3,700	\$ 3,250	\$ 2,910
Proven non-producing	31	5,890	620	3,080	2,480	2,030
Probable	287	4,880	775	5,400	4,210	3,390
<b>Total</b>	<b>566</b>	<b>12,800</b>	<b>1,846</b>	<b>\$12,180</b>	<b>\$ 9,940</b>	<b>\$ 8,330</b>

### Reserves Reconciliation

	Oil & NGLs (mbbls)			Gas (mmcf)			BOE (mboe)		
	Proven	Probable	Total	Proven	Probable	Total	Proven	Probable	Total
January 1, 1995	130	148	278	1,504	1,591	3,095	280	307	587
Acquisitions	159	48	207	220	268	488	181	75	256
Discoveries	0	0	0	158	52	210	16	5	21
Production	(28)	—	(28)	(36)	—	(36)	(32)	—	(32)
Revisions	(37)	(131)	(168)	(39)	(141)	(180)	(41)	(145)	(186)
<b>January 1, 1996</b>	<b>224</b>	<b>65</b>	<b>289</b>	<b>1,807</b>	<b>1,770</b>	<b>3,577</b>	<b>404</b>	<b>242</b>	<b>646</b>
Acquisitions	44	147	191	4,814	2,094	6,908	525	356	881
Discoveries	48	39	87	1,341	885	2,226	182	128	310
Production	(52)	—	(52)	(175)	—	(175)	(69)	—	(69)
Revisions	15	36	51	133	131	264	29	49	78
<b>January 1, 1997</b>	<b>279</b>	<b>287</b>	<b>566</b>	<b>7,920</b>	<b>4,880</b>	<b>12,800</b>	<b>1,071</b>	<b>775</b>	<b>1,846</b>

## Finding and Development Costs

Finding and development costs are a key measure of corporate profitability. Focusing in well-defined areas resulted in a reduction of finding and development costs in 1996, a trend we expect will continue through 1997. BXL calculates finding and development costs based on total capital expenditures, including land, seismic, drilling, equipping and facilities costs, divided by reserve additions. The calculations do not include future development costs associated with bringing non-producing reserves on-stream, estimated to be \$2.7 million at January 1, 1997.

Capital Expenditures (thousands)	Since Inception	1996
Total exploration and development costs, excluding acquisitions	\$ 3,558	\$ 1,785
Acquisition costs	4,898	2,203
Total finding and development costs	8,456	3,988
Office equipment	91	33
Total capitalized costs (net of dispositions)	\$ 8,547	\$ 4,021

Reserves Additions (mboe)		
Exclusive of acquisitions		
Proven	268	182
Proven plus probable	523	310
Including acquisitions		
Proven	1,171	736
Proven plus probable	1,946	1,269

Finding and Development Costs (per boe)		
Exclusive of acquisitions		
Proven	\$ 13.28	\$ 9.81
Proven plus probable	\$ 6.80	\$ 5.76
Including acquisitions		
Proven	\$ 7.22	\$ 5.42
Proven plus probable	\$ 4.35	\$ 3.14

## Reserves Pricing Forecast

### Pricing Assumptions\*

	WTI Crude Oil (\$US per bbl)	Edmonton Light Oil (\$Cdn per bbl)	Alberta Spot Gas (\$Cdn per mmbtu)
1997	21.00	27.25	1.65
1998	19.00	24.75	1.70
1999	20.00	26.00	1.85
2000	21.00	27.25	2.00
2001	21.50	28.00	2.25
2002	22.00	28.75	2.35
2003	22.50	29.50	2.50
2004+	+2%/yr	+2%/yr	+2%/yr

\* Based on Gilbert Laustsen Jung Associates Ltd. base case price forecast effective January 1, 1997.

## Results of Operations

### Analysis of Statement of Operations

	Oil & NGLs		Gas		Total	
	1996	1995	1996	1995	1996	1995
<b>Sales volumes</b>	(bbls)		(mcf)		(boe)	
Annual	52,189	28,262	175,066	35,530	69,696	31,815
Average daily	143	77	478	97	191	87
<b>Revenues and expenses (thousands)</b>						
Sales	\$ 1,480	\$ 642	\$ 295	\$ 42	\$ 1,775	\$ 684
Royalties (net of ARTC)	(357)	(195)	(41)	(4)	(398)	(199)
Production expenses	(426)	(136)	(78)	(4)	(504)	(140)
Operating profit	\$ 697	\$ 311	\$ 176	\$ 34	\$ 873	\$ 345
<b>Netbacks</b>						
	(per bbl)		(per mcf)		(per boe)	
Selling price	\$ 28.36	\$ 22.73	\$ 1.69	\$ 1.17	\$ 25.47	\$ 21.50
Royalties (net of ARTC)	(6.84)	(6.91)	(0.23)	(0.10)	(5.71)	(6.25)
Production expenses	(8.18)	(4.82)	(0.44)	(0.12)	(7.24)	(4.42)
Operating netback	\$ 13.34	\$ 11.00	\$ 1.02	\$ 0.95	\$ 12.52	\$ 10.83
Gas management contracts					13.58	12.96
General and administrative					(5.31)	(9.50)
Interest (net)					(1.44)	0.26
Depletion, depreciation and amortization					(7.89)	(7.83)
Deferred taxes					(3.27)	-
Corporate netback					\$ 8.19	\$ 6.72

### OIL OPERATIONS

The 86 percent increase in average daily oil production is a result of new production at Gift/Little Horse and Wilson Creek, partially offset by declines at Kisbey/Redvers. The Gift/Little Horse property generated production revenue for 12 months of 1996, compared to three months in 1995. Wilson Creek production commenced in July 1996.

BXL's average oil price increased 25 percent during 1996 to \$28.36 per barrel as a result of the 20 percent increase in the benchmark West Texas Intermediate average oil price and the increase in production of high quality crude from Gift/Little Horse. BXL entered into one oil hedging transaction during 1996 that, when compared to spot prices, resulted in a \$26,000 decrease in oil revenues and cash flow.

Oil royalties decreased to 24 percent of sales in 1996 from 30 percent in 1995. The decrease is primarily due to our reduced dependence on production from the Kisbey/Redvers property which is burdened with relatively high royalties. Royalties as a percentage of sales are expected to decline in 1997 as a result of the ongoing change in our production profile.

Oil production expenses rose substantially in 1996 to \$8.18 per barrel, up from \$4.82 per barrel in 1995. This increase is due primarily to the exceptionally high lifting costs experienced in the Little Horse area where produced oil and water must be trucked from well sites to a central facility. During 1997, operating costs at Little Horse should be reduced as marginal producers are shut-in and more productive wells are pipelined to facilities.

#### Summary of Average Daily Production by Area

	Oil & NGLs (bbbls per day)			Gas (mcf per day)		
	1996	1995	% Change	1996	1995	% Change
Gift/Little Horse	94	18	422	—	—	—
Tweedie	—	—	—	58	—	—
Wilson Creek/Westerose	7	—	—	192	—	—
Kisbey/Redvers	42	59	(29)	—	—	—
Sugden	—	—	—	228	97	135
	143	77	86	478	97	393

#### NATURAL GAS OPERATIONS

The near four-fold increase in average daily natural gas production to 478 thousand cubic feet per day is the result of new production at Wilson Creek, which was acquired in July 1996 and at Tweedie, which started up in November 1996. In addition, the Sugden property produced natural gas for 12 months in 1996 compared to three months in 1995.

BXL benefited by the general increase in western Canadian gas prices during 1996, averaging \$1.69 per thousand cubic feet of natural gas sold, compared to \$1.17 in 1995. During 1996, BXL balanced its natural gas sales among long-term, short-term and daily spot price sales contracts.

BXL's average natural gas royalty rate increased to 14 percent of sales in 1996, up from ten percent in 1995. During 1995, all of BXL's gas production came from the Sugden area which benefits from a reduction in Crown royalties due to the Alberta Royalty Tax Credit program. Our 1996 production from Wilson Creek and most of the Tweedie production does not qualify for this program. As a percentage of sales, 1997 natural gas royalties are expected to approximate 1996 rates.

Natural gas production expenses increased to \$0.44 per thousand cubic feet in 1996 from \$0.12 per thousand cubic feet in 1995. Production from the Sugden property, which accounted for 100 percent of BXL's 1995 gas production does not require processing. Forty percent of our 1996 gas production came from the Wilson Creek property, where the extraction of natural gas liquids requires extensive processing. Overall natural gas operating expenses were also higher in 1996 due to costs associated with the commencement of production at Tweedie.

## GAS MANAGEMENT CONTRACT OPERATIONS

BXL is the agent for two U.S.-based power generation facilities, managing their long-term Canadian natural gas supply. As agent, BXL does not own pipeline capacity nor do we sell our gas reserves to the facilities. The company earns a fee based on natural gas volumes shipped and participates in profits generated from the management of unused, prepaid pipeline transportation. BXL acquired the existing gas management contracts in 1993. Until the end of 1996, administration of the contracts had been subcontracted to a Calgary-based gas marketing company. In December 1996, BXL assumed direct operatorship of the contracts.

During 1996, gas management contract fees increased 167 percent to \$946,000 from \$354,000 in 1995. Managing available pipeline capacity during periods of relatively high gas price differential between western Canada and the northeast United States was the primary reason for the increase. Although 1995 results were less than expected, 1996 results were extraordinary.

## GENERAL AND ADMINISTRATIVE EXPENSES

BXL is an emerging company and our overhead levels reflect a continuous balance between maintaining a low-cost operation and building a growth-oriented management team. As the company grows, we expect total overhead to increase moderately, the percentage capitalized to decrease and most importantly, a year over year decline in overhead costs incurred per unit of production.

### General and Administrative Expenses

(thousands)	1996			1995		
		% of total	per boe		% of total	per boe
Expensed	\$ 370	77%	\$ 5.31	\$ 302	70%	\$ 9.50
Capitalized	111	23%	1.59	130	30%	4.09
Total	\$ 481	100%	\$ 6.90	\$ 432	100%	\$ 13.59

## INTEREST EXPENSES

Interest expense was \$106,000 in 1996 as compared to \$21,000 in 1995. BXL's 1996 cash flow was 13 times interest expense. During 1996, BXL carried average bank debt of \$911,000 at an average interest rate of seven percent and \$450,000 of nine percent convertible debentures. The company's long-term debt was minimal until the last quarter of 1995.

## DEPLETION, DEPRECIATION AND AMORTIZATION EXPENSES

The 121 percent increase in depletion, depreciation and amortization expense to \$550,000 in 1996 is almost exclusively due to higher production volumes. Calculated on a barrel of oil equivalent basis, this expense is expected to decline in 1997, as the results of lower finding costs are reflected in the calculation.

## Depletion, Depreciation and Amortization Expense

(thousands)	1996 per boe		1995 per boe	
Depletion and depreciation of oil and gas properties	\$ 507	7.27	\$ 221	6.95
Provision for future site restoration	20	0.29	15	0.46
Depreciation of office equipment	14	0.20	11	0.36
Amortization of gas management contracts	9	0.13	2	0.06
Total provision	\$ 550	7.89	\$ 249	7.83

## TAXES

BXL did not pay current income taxes in 1996 and our liability for 1997 income taxes will depend somewhat on the nature and magnitude of the company's 1997 capital expenditure program. Pursuant to the terms of flow-through share arrangements, income tax deductions relating to approximately \$1,300,000 of expenditures to be incurred in 1997 were renounced to subscribers effective December 31, 1996.

## Future Tax Deductions

(thousands)	1996	1995	Deduction Rate
Canadian exploration expenses	\$ 520	\$ 536	100%
Canadian development expenses	330	386	30%
Canadian oil and gas property expenses	3,253	1,854	10%
Undepreciated capital costs	1,570	625	20-30%
Other	68	50	20%
	\$ 5,741	\$ 3,451	

## CAPITAL EXPENDITURES

Consistent with BXL's strategy of building core areas, property acquisitions accounted for 52 percent of our 1996 capital expenditure program and 72 percent of our 1995 program. In September 1995, we acquired the Gift/Little Horse property, which became our second core area. Wilson Creek/Westerose became our third core area with the completion of our initial acquisition in July 1996 and an acquisition to expand our Tweedie interests was completed in December 1996. BXL plans to invest up to \$4 million on existing properties during 1997, approximately half of which will be directed to facilities and equipment.

## Capital Expenditures

(thousands)	1996	1995
Property acquisitions	\$ 2,203	\$ 1,552
Land and lease retention	229	40
Geological and geophysical	110	32
Drilling and completion	820	214
Production equipment and facilities	752	177
Capitalized overhead and other	111	130
Office furniture and equipment	33	11
Total expenditures	\$ 4,258	\$ 2,156
Dispositions*	(237)	-
Net expenditures	\$ 4,021	\$ 2,156

## Liquidity and Capital Resources

At December 31, 1996, BXL's long-term financial commitments consisted of bank debt of \$1,162,000 compared to \$689,000 in 1995, and convertible debentures of \$450,000 which is unchanged from 1995. The company's bank credit facility totals \$1,975,000, including a \$1,375,000 revolving production loan and a \$600,000 demand loan. No principal repayments are required, provided certain financial ratios and covenants are maintained. Although BXL expects its bank facility to increase in 1997, our strategy is to limit long-term debt to less than two times annualized cash flow.

During 1996, BXL raised \$1,850,000 of new equity through the issuance of 3,400,000 shares at prices ranging from \$0.45 to \$0.67 per share. At December 31, 1996 the company had 16,999,155 shares outstanding and 3,037,500 shares reserved for future issuance.

### Capital Resources

(thousands)	1996	1995
Cash flow from operations	\$ 1,349	\$ 463
Change in non-cash working capital	14	(148)
Issues of common shares (net of costs)	1,811	370
Increase in bank debt	473	500
Cash	374	513
Issue of convertible debentures	—	450
Other	—	8
	<b>\$ 4,021</b>	<b>\$ 2,156</b>

## Business Risks and Prospects

The company is subject to operational risks including finding and developing oil and gas reserves in economic quantities, fluctuations in production performance, marketing of reserves and environmental hazards. Our primary means of mitigating these risks is to employ highly qualified personnel, either directly as employees or indirectly when contracting for services. Our philosophy of operating in a limited number of core areas allows us to develop a high level of operational and managerial expertise in each area. BXL also reduces risk through the use of new technology in the field and in corporate offices, as well as by carrying adequate levels of insurance.

BXL expects 1997 to be another year of high activity and improved operating results. As production grows, increases in cash flow will provide the company with additional capital to exploit the opportunities built in 1996. Moreover, increases in production will lead to efficiencies as corporate costs decrease on a per unit basis.

## Management's Report

All of the information in this annual report is the responsibility of management. The accompanying financial statements of BXL Energy Ltd. have been prepared by management in accordance with Canadian generally accepted accounting principles. The financial information elsewhere in the annual report has been reviewed to ensure consistency in all material respects with that in the financial statements.

BXL Energy Ltd. maintains appropriate systems of internal control to give reasonable assurance that transactions are appropriately authorized, assets are safeguarded from loss or unauthorized use and financial records provide reliable and accurate information for the preparation of financial statements.

KPMG, an independent firm of Chartered Accountants, has been engaged to examine the financial statements and provide their Auditors' Report. Their report is presented with the financial statements.

The Directors are responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Directors exercise this responsibility through the Audit Committee. This committee, which is comprised of non-management Directors, meets with management and the external auditors to satisfy itself that management responsibilities are properly discharged and to review the financial statements before they are presented to the Directors for approval. The financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.



Michael J. Makinson  
Vice President, Finance and  
Chief Financial Officer

## Auditors' Report to the Shareholders

We have audited the balance sheets of BXL Energy Ltd. as at December 31, 1996 and 1995 and the statements of operations and retained earnings and changes in financial position for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1996 and 1995 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.



Chartered Accountants

Calgary, Canada  
March 17, 1997

## BALANCE SHEETS

at December 31,

1996

1995

## ASSETS

## Current assets

Cash	\$	—	\$	373,515
Accounts receivable		719,975		303,993
		719,975		677,508
Property and equipment (Note 2)		6,371,984		3,585,333
Gas management contracts		1		8,960
	\$	7,091,960	\$	4,271,801

## LIABILITIES

## Current liabilities

Accounts payable and accrued liabilities	\$	711,978	\$	281,736
		711,978		281,736
Bank loan (Note 3)		1,162,124		688,870
Convertible debentures (Note 3)		450,000		450,000
Deferred income taxes		228,000		—
Provision for site restoration costs		63,000		43,000
		2,615,102		1,463,606

## SHAREHOLDERS' EQUITY

Share capital (Note 4)		3,903,994		2,806,312
Retained earnings		572,864		1,883
		4,476,858		2,808,195

## Subsequent events (Note 4)

\$ 7,091,960

\$ 4,271,801

See accompanying notes

On behalf of the Board of Directors



Director



Director

## STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

years ended December 31,	1996	1995
<b>REVENUES</b>		
Oil and gas sales	\$ 1,775,472	\$ 683,990
Royalties	(397,671)	(198,746)
	<b>1,377,801</b>	<b>485,244</b>
Gas management contract fees	<b>946,465</b>	<b>354,187</b>
Gain on disposition of gas management contract rights (Note 8)	—	58,241
Interest	<b>2,843</b>	<b>28,878</b>
	<b>2,327,109</b>	<b>926,550</b>
<b>EXPENSES</b>		
Production	<b>504,397</b>	<b>140,498</b>
General and administrative	<b>370,140</b>	<b>302,378</b>
Interest	<b>103,591</b>	<b>20,649</b>
Depletion, depreciation and amortization	<b>550,000</b>	<b>249,000</b>
	<b>1,528,128</b>	<b>712,525</b>
<b>EARNINGS BEFORE INCOME TAXES</b>	<b>798,981</b>	<b>214,025</b>
<b>DEFERRED INCOME TAXES (Note 5)</b>	<b>228,000</b>	<b>—</b>
<b>NET EARNINGS</b>	<b>570,981</b>	<b>214,025</b>
<b>RETAINED EARNINGS, BEGINNING OF YEAR</b>	<b>1,883</b>	<b>(212,142)</b>
<b>RETAINED EARNINGS, END OF YEAR</b>	<b>\$ 572,864</b>	<b>\$ 1,883</b>
<b>NET EARNINGS PER SHARE (Note 6)</b>		
Basic	\$ 0.04	\$ 0.02
Fully diluted	\$ 0.04	\$ 0.02

See accompanying notes

## STATEMENTS OF CHANGES IN FINANCIAL POSITION

years ended December 31,

1996

1995

## CASH PROVIDED BY (USED FOR)

## OPERATIONS

Net earnings	\$ 570,981	\$ 214,025
Add charges not affecting cash		
Depletion, depreciation and amortization	550,000	249,000
Deferred income taxes	228,000	—
Cash flow from operations	1,348,981	463,025
Net change in non-cash working capital	14,260	(148,039)
	1,363,241	314,986

## FINANCING

Issue of common shares	1,850,000	378,000
Increase in bank loan	473,254	500,070
Issue of convertible debentures	—	450,000
Redemption of class B non-voting shares (Note 8)	—	(1)
Share issue costs	(38,718)	(7,903)
	2,284,536	1,320,166

## INVESTING

Expenditures on property and equipment	(4,258,454)	(2,156,145)
Proceeds on sale of property and equipment	237,162	—
Other assets	—	7,700
	(4,021,292)	(2,148,445)

DECREASE IN CASH (373,515) (513,293)

CASH, BEGINNING OF YEAR 373,515 886,808

CASH, END OF YEAR \$ — \$ 373,515

## CASH FLOW FROM OPERATIONS PER SHARE

(Note 6)

Basic	\$ 0.09	\$ 0.03
Fully diluted	0.08	0.03

See accompanying notes

Years ended December 31, 1996 and 1995

BXL Energy Ltd. is engaged in the acquisition, exploration, development and production of petroleum and natural gas reserves in western Canada. In addition, the company is the agent for two U.S.-based power generation facilities and manages their Canadian sourced natural gas supply.

## 1. Significant accounting policies

### (a) Petroleum and natural gas operations

The company follows the full cost method of accounting for petroleum and natural gas operations whereby all costs related to the exploration for and development of petroleum and natural gas reserves are capitalized into a single cost centre. Such costs include those related to lease acquisition, geological and geophysical activities, lease rentals on non-producing properties, drilling of productive and non-productive wells, tangible production equipment, and that portion of general and administrative expenses directly attributable to exploration and development activities. Proceeds received from the disposal of properties are normally deducted from the full cost pool without recognition of a gain or loss. When a significant portion of properties is sold, a gain or loss is recorded and reflected in the statement of operations.

Costs of acquiring unproved properties are initially excluded from the full cost pool and are assessed yearly to ascertain whether impairment has occurred. When proved reserves are assigned to the property or the property is considered to be impaired, the cost of the property or the amount of impairment is added to the full cost pool. Depletion of petroleum and natural gas properties and depreciation of production equipment are calculated using the unit-of-production method based upon estimated proved reserves, before royalties, as determined by an independent engineer. For purposes of the calculation, natural gas reserves and production are converted to equivalent volumes of petroleum based upon relative energy content.

The company annually applies a ceiling test to capitalized costs to ensure that such costs do not exceed the cost of unproved properties plus undiscounted future net revenues from production of proved reserves at year end product prices less future administrative, financing, site restoration and income tax expenses. Where a ceiling test deficiency occurs and is related to significant acquisitions within the last 24 months, and is not permanent, a write-down of petroleum and natural gas properties is not required.

Future site restoration costs are amortized using the unit-of-production method. These costs are based on year-end estimates of the anticipated costs of site restoration.

### (b) Joint ventures

Substantially all of the company's exploration and production activities are conducted jointly with others. These financial statements reflect only the company's proportionate interest in such activities.

### (c) Measurement uncertainty

The amounts recorded for depletion and depreciation of property and equipment and the provision for future site restoration costs are based on estimates. The ceiling test calculation is based on estimates of proved reserves, production rates, oil and natural gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant.

## 1. Significant accounting policies (continued)

### (d) Flow-through shares

The resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share arrangements are renounced to investors. To recognize the foregone tax benefits to the company, the carrying value of the oil and gas properties acquired and the shares issued are recorded net of the tax benefits renounced to shareholders.

### (e) Alberta Royalty Tax Credit

Alberta Royalty Tax Credit is recorded as a reduction of royalties paid.

## 2. Property and equipment

	1996	1995
Petroleum and natural gas properties	\$ 8,456,704	\$ 4,468,688
Tax benefits renounced	(943,600)	(230,000)
Office furniture and equipment	90,623	57,347
	7,603,727	4,296,035
Less accumulated depletion and depreciation	(1,231,743)	(710,702)
	\$ 6,371,984	\$ 3,585,333

As at December 31, 1996 costs of \$677,392 (1995 – \$521,376) associated with unproved properties have been excluded from the depletion and depreciation calculation. During 1996, the company capitalized \$111,097 (1995 – \$129,771) of general and administrative expenses relating to exploration and development activities.

As a result of a ceiling test calculation, which was performed with an effective date of December 31, 1996, it was determined that the net recoverable amount calculated under the full cost accounting guideline exceeded the net book value of the company's petroleum and natural gas properties. The prices used in the ceiling test calculation of December 31, 1996 were \$33.20 (1995 – \$23.58) per barrel of crude oil and \$2.25 (1995 – \$1.31) per thousand cubic feet of natural gas. The ceiling test is a cost recovery test and is not intended to result in an estimate of fair market value.

The provision for future site restoration costs is recorded in the statement of operations as a component of depletion and depreciation (1996 – \$20,000; 1995 – \$14,655) and on the balance sheet as a long-term liability. At December 31, 1996, the estimated future site restoration costs to be accrued over the life of the remaining proved reserves are approximately \$412,000 (1995 – \$252,000).

### 3. Long-term debt

	1996	1995
Bank loan	\$ 1,162,124	\$ 688,870
Convertible debenture	450,000	450,000
	\$ 1,612,124	\$ 1,138,870

#### BANK LOAN

The company has a \$1,975,000 loan facility available with a Canadian chartered bank comprised of a \$1,375,000 revolving reducing production loan and a \$600,000 demand loan. The loans, which bear interest at the bank prime rate plus one half of 1% per annum, are secured by a \$2,000,000 demand debenture which provides a first floating charge on all real and personal property of the company, an assignment of book debts and an undertaking to provide additional fixed charge security if required by the bank. The loans are subject to annual review and have a demand feature; however, repayments are not required provided that borrowings do not exceed the borrowing base and other loan covenants are complied with. The company can utilize the facility through direct borrowings from the bank or through Bankers Acceptances.

The December 31, 1996 balance of \$1,162,124 includes Bankers Acceptances of \$979,100 at a rate of approximately 6.4 percent. The December 31, 1995 balance of \$688,870 is comprised of Bankers Acceptances at a rate of 7.75 percent.

#### CONVERTIBLE DEBENTURES

The unsecured convertible redeemable debentures were issued on December 15, 1996 and bear interest at a rate of 9 percent per annum. The principal is due on December 31, 2000 with interest payable semi-annually. The debentures are convertible at the option of the holder at any time into common shares of the company at a conversion price of \$0.40 per share. The company can redeem the debentures after June 30, 1998 provided the common shares of the company have traded for 20 consecutive days at a price equal to or greater than \$0.60 per share.

### 4. Share capital

#### AUTHORIZED

Unlimited number of common shares, no par value

Unlimited number of first preferred shares, no par value

Unlimited number of second preferred shares, no par value

#### 4. Share capital (continued)

##### ISSUED

	1996		1995	
	Number of shares	Amount	Number of shares	Amount
<b>Common shares</b>				
Balance, beginning of year	13,599,155	\$ 2,806,312	12,654,155	\$ 2,606,215
Private placement for cash	500,000	250,000	—	—
Private placements on a flow-through basis for cash	2,900,000	1,600,000	945,000	378,000
Tax benefit relating to renounced expenditures	—	(713,600)	—	(170,000)
Share issue costs	—	(38,718)	—	(7,903)
	16,999,155	\$ 3,903,994	13,599,155	\$ 2,806,312
<b>Class B non-voting shares</b>				
Balance, beginning of year	—	—	1,260,000	1
Redemption of outstanding shares	—	—	(1,260,000)	(1)
	—	—	—	—
Balance, end of year		\$ 3,903,994		\$ 2,806,312

##### SHARE CAPITAL OFFERINGS

During 1996, the company completed a total of four private placements. In June, 1,000,000 flow-through common shares were issued at \$0.45 per share for proceeds of \$450,000. In November, 500,000 common shares were issued at \$0.50 per share for proceeds of \$250,000. In December, two placements of flow-through common shares were completed whereby 1,000,000 shares were issued at \$0.55 per share for proceeds of \$550,000 and 900,000 shares at \$0.667 per share were issued for proceeds of \$600,000. Pursuant to the flow-through share offerings, the company renounced \$1,600,000 of qualifying expenditures effective December 31, 1996, of which \$1,300,000 will be incurred in 1997.

In February 1995, the company completed a \$378,000 private placement of units at a price of \$0.40 per unit, each unit being comprised of one flow-through common share and one-half of one non-transferrable common share purchase warrant. Pursuant to the offering, the company issued 945,000 flow-through shares and 472,500 share purchase warrants.

##### STOCK OPTIONS

At December 31, 1996, options to purchase 1,440,000 common shares of the company at \$0.40 per share were outstanding. In January 1997, 230,000 options exercisable at \$0.60 per share were granted.

##### WARRANTS

At December 31, 1996, 472,500 common share purchase warrants were outstanding. Each warrant entitled the holder to acquire one common share of the company for \$0.55 per share prior to February 23, 1997. Subsequent to year end, 391,250 warrants were exercised for proceeds of \$215,188.

## 5. Income taxes

The provision for income taxes differs from the result which would be obtained by applying the combined Canadian federal and provincial income tax rate to earnings before income taxes. The principal reasons for this difference are as follows:

	1996	1995
Earnings before income taxes	\$ 571,000	\$ 214,000
Corporate tax rate	44.6%	44.6%
Computed income tax expense	255,000	95,000
Increase (decrease) resulting from:		
Recognition of loss not previously recognized	(112,000)	(133,000)
Non deductible crown payments, net	130,000	55,000
Resource allowance	(46,000)	(9,000)
Other	1,000	(8,000)
Income tax provision	\$ 228,000	\$ -

## 6. Per share data

Per share amounts are based on the weighted average number of common shares outstanding during the period, which for 1996 was 14,261,175 shares (1995 – 13,477,470 shares). The imputed interest rate used for purposes of the fully diluted earnings and cash flow from operations per share calculation is 5 percent (1995 – 6 percent).

## 7. Financial instruments

The carrying value of the company's financial assets and liabilities approximates their fair values at December 31, 1996 and 1995.

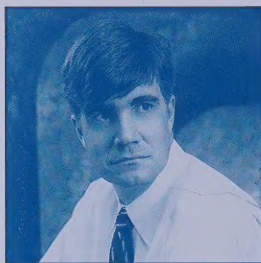
## 8. Related party transactions

Two directors of the company are officers, and directors of Brymore Energy Ltd. (a private Alberta corporation).

The gas management contract operations of the company were purchased from a limited partnership related to Brymore in 1993, resulting in the partnership acquiring 4,410,000 common shares and 1,260,000 class B non-voting shares of the company. Coincident with this transaction, the company entered into an agreement with Brymore to provide for the operation and administration of the gas management contracts. The compensation to Brymore consisted of a fixed monthly fee; a percentage of certain revenues and reimbursement of specified expenses. For 1996, the company recorded net gas management contract fees of \$946,465 (1995 – \$354,187) after the payment of Brymore's compensation of \$238,875 (1995 – \$124,737).

In mid December 1996, the arrangement with Brymore was terminated and the company began operating the management contracts directly.

In 1995, the company entered into an arrangement with Brymore and a related limited partnership whereby the company agreed to relinquish its rights to a non-operating gas management contract and to cancel a non-competition agreement executed in favour of the company. In consideration the company received \$58,240 and a 10 percent net profit interest in specified gas marketing arrangements entered into by Brymore and related parties. Furthermore, the company redeemed all 1,260,000 class B non-voting shares outstanding for \$1. This transaction resulted in a gain of \$58,241 which is recognized in the 1995 statement of operations.



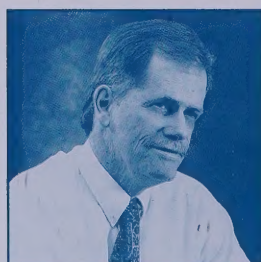
**BRUCE G. MCINTYRE, President**

Bruce, a founder of BXL, has a BSc. (Honours) in Geology from Carleton University. With over 20 years of progressive experience primarily with independent exploration and production companies, he has established a proven track record of adding reserves and production. His extensive experience spans the Western Canadian Sedimentary Basin, with particular success in central Alberta and the Peace River Arch area of northern Alberta. Bruce is a member of APEGGA, the Canadian Society of Petroleum Geologists and the American Association of Petroleum Geologists.



**MICHAEL J. MAKINSON, Vice President, Finance**

Michael, a founder of BXL, has a B.Comm from the University of Calgary. He has over 16 years of diverse experience, primarily with publicly listed oil and gas companies. Michael's areas of expertise include corporate combinations, equity and debt financing and asset acquisitions and dispositions. He is also responsible for communication to BXL's stakeholders and serves as the company's corporate secretary. Michael is a member of the Institute of Chartered Accountants of Alberta.



**DAVID B. SAVAGE, Vice President, Land**

Dave has been with BXL since July 1996 and has a B.A. in Economics from the University of Calgary. He brings 22 years of petroleum industry experience in exploration, production, operations and senior management to BXL where his primary responsibilities are the negotiation and documentation of BXL's land, joint ventures and marketing matters. Dave is a Director of the Small Explorers and Producers Association of Canada, Vice Chair of the Calgary Chamber of Commerce Alternative Dispute Resolution Committee and an active member (past President) of the Petroleum Joint Venture Association and the Canadian Association of Petroleum Landmen.





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